DOCUMENT RESUME

ED 282 484 HE 020 299

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TITLE	The Permissibility of Withholding Transcripts under the Bankruptcy Law. NACUA Publication Series.
INSTITUTION	National Association of Coll. and Univ. Attorneys, Washington, D.C.
SPONS AGENCY	Ford Foundation, New York, N.Y.
PUB DATE	Jul 86
NOTE	8p.
AVAILABLE FROM	National Association of College and University Attorneys, One Dupont Circle, NW, Suite 620, Washington, DC 20036 ($3.50, prepaid).
PUB TYPE	Viewpoints (120)
EDRS PRICE	MF01 Plus Postage. PC Not Available from EDRS.
DESCRIPTORS	*Academic Records; *College Students; Compliance (Legal); Higher Education; *Legal Responsibility; *Loan Repayment; *Registrars (School)
IDENTIFIERS	*Bankruptcy; *Debt (Financial)

ABSTRACT

Provisions of the U.S. Bankruptcy Code that affect the right of colleges to withhold transcripts as a means of collecting student debts are considered. Automatic stay provisions state that the filing of a petition for bankruptcy relief prohibits actions to collect obligations of the debtor. The discharge injunction provides that once a discharge of debts has been granted, further actions to collect are barred. In addition, antidiscrimination clauses prevent public entities, and, in some respects, private entities from denying various privileges to persons seeking bankruptcy protection. Three rules to follow are cited: (1) Do not withhold a transcript during the pendency of a bankruptcy action without acquiring relief from the stay. (2) If a discharge of all debts has been granted to the debtor, schools should not deny access to, or orders of, transcripts. (3) It is permissible to deny transcripts where the case is no longer pending before the court and educational debts were not discharged, especially if the underlying obligation is a student loan. (SW)

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The Permissibility of Withholding Transcripts Under the Bankruptcy Law

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The Permissibility of Withholding Transcripts Under Bankruptcy Law

Introduction

The United States Congress has exercised its constitutional power to provide for uniform laws of bankruptcy, thereby permitting federal courts to intervene in what are essentially matters of state law. The Bankruptcy Code provides for restraint on the actions of creditors to ensure the integrity of bankruptcy law. Those restraints which affect the right of colleges and universities to withhold transcripts as a means of collecting student debts are the topic of this pamphlet.[1]

The purpose of bankruptcy law is to seek the fairest possible adjustment between overextended debtors and their creditors. Bankruptcy law requires debtors to distribute their property or income, excepting living necessities, to their creditors. To the extent that debts are not paid off through distribution, they are discharged. The effect of discharge is that the claim for the debt is no longer legally enforceable. There are three kinds of bankruptcy relevant here: chapter 7 bankruptcies, in which the non-exempt property of the debtor is liquidated and the proceeds are distributed among the creditors; chapter 11 bankruptcies, in which the debtor's financial affairs are reorganized under a court-approved plan; and chapter 13 bankruptcies, under which debtors with regular income devote a portion of their income to paying debts.

Three sets of provisions of the Bankruptcy Code affect the right to withhold transcripts. The first are the automatic stay provisions[2]

1. Users of this pamphlet should be aware that the advice given here is general in nature. The specific facts of your case and the specific jurisdiction in which the case arises may affect the choice of legal alternatives. Your legal counsel should be consulted for specific advice.

2. §362 (a) (6), and in chapter 13 bankruptcies, §1301. References to sections are to the 1978 Bankruptcy Code as amended, Title 11, United States Code.

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This publication is funded by a grant from The Ford Foundation.

Printed in the United States

which state that the filing of a petition for bankruptcy relief acts as a prohibition of actions to collect obligations of the debtor. The second, the discharge injunction, provides that once a discharge of debts has been granted, further actions to collect are barred.[3] Finally, the anti-discrimination clauses prevent public entities, and, in some respects, private entities, from denying various privileges to persons seeking bankruptcy protection.[4] Together these provisions forbid the withholding of transcripts during the pendency of a bankruptcy action and afterward if all debts have been discharged. However, if debts are not discharged, withholding transcripts is permissible once the bankruptcy action is final.

Prohibition of Withholding Transcripts During the Pendency of a Bankruptcy Proceeding: The Automatic Stay

Restrictions on the actions of creditors begin with the filing of a bankruptcy petition. A petition for bankruptcy prohibits the creditor from taking any action to recover the claim from the debtor.[5] In addition, if the debtor has filed under chapter 13, section 1301 prohibits actions to collect a consumer debt from a codebtor, even though the codebtor has not sought protection under bankruptcy law.[6] The stay provisions prohibit withholding transcripts during a bankruptcy proceeding unless the court has lifted the stay.

Creditors should receive formal notice of the bankruptcy petition and stay from the court soon after the case begins. However, even if no formal notice is received, but the creditor is made aware through other channels, no action should be taken to collect without first confirming with the proper court that no action is pending. Often debtors themselves will inform creditors that a bankruptcy petition has been filed. Because the stay is in effect regardless of whether formal notice of it has been received, it is wise not to treat such information casually.

The purposes of the stay are to prevent creditors from gaining an unfair advantage over one another in order to assure fair treatment among creditors, and to provide breathing room for the debtor. To effectuate these goals, courts tend to interpret the stay provisions broadly.

It is well established under the 1978 Bankruptcy Code that refusal to release transcripts violates the stay.[7] An older case holding that withholding transcripts was permissible under the 1898 Bankruptcy Act was legislatively overruled by the new code.[8] Violation of the stay could subject the institution to payment of damages, attorneys' fees and, in egregious cases, punitive damages.[9]

The court may grant relief from the stay against the debtor; however, in nearly all cases involving student debts, such relief will not be available because relief is generally warranted only where failure to grant it will result in irreparable harm to the creditor.[10] Relief from

3. §524 (a) (2).

4. §525 (a) and (b).

5. §362 (a) (6).

6. §1301. A codebtor is a person who is liable with the debtor or who secured the debt. Thus, if parents take out an educational loan for a student and the student is a co-maker or guarantor, a chapter 13 petition filed by the parents may stay actions to recover from the student. In some cases there is a question whether §1301 is applicable to student debts. One court has ruled that a loan for funds to be used for business training is not a "consumer debt" as required by §1301. See, §101 (7). The court lifted the codebtor stay in that case. *In re Chrisman*, 27 B.R. 648 (Bkrtcy S.D. Ohio 1982). It could be argued on the basis of this case that the codebtor stay is not applicable to student loans for employment-related training. However, in most cases, even where the education leads to a professional degree, the debt should be treated as a consumer debt.

7. *E.g., In re Parham*, 56 B.R. 531 (Bkrtcy E.D. Va. 1986); *In re Reese*, 38 B.R. 681, 683 (Bkrtcy N.D. Ga. 1984).

8. In *Girardier v. Webster College*, 563 F.2d 1267 (8th Cir. 1977), the court held that section 32 (f)(2) of the 1898 act did not prevent non-judicial attempts to collect on obligations. *See Parham*, 56 B.R. at 532-3 for a discussion of the reasons for concluding that *Girardier* was overruled.

9. §362 (h).

10. §362 (d).

the codebtor stay in chapter 13 cases is more readily available. The creditor may gain relief from the stay as against the codebtor to the extent that the codebtor was the recipient of the college's services, to the extent that the debtor does not plan to pay all of the debt or where the college is likely to suffer irreparable harm.[11] Without positive action from the court, the stay lasts until the case is closed, dismissed or a discharge is granted or denied, whichever occurs first.[12] The stay could remain in effect for years. For example, chapter 13 plans may extend as long as five years.[13]

Post-Discharge Restrictions on Withholding Transcripts: The Discharge Injunction

If the debtor has been discharged from all debts owed to a creditor, the discharge injunction[14] prevents any action to recover the debts. Among the actions prohibited is the withholding of transcripts. However, it is often not easy to tell whether a debtor has been discharged from educational loans. Thus, it is important to determine first whether the loan has been discharged.

To determine whether educational loans have been discharged,[15] it is necessary to obtain a copy of the discharge and any rulings on the dischargeability of debts. If the discharge is entered under chapter 7, and if there has been no ruling on the dischargeability of the loan, in most jurisdictions the discharge will not affect the loan.[16] Similarly, a discharge under a chapter 13 plan which has not been completed,[17] or under chapter 11, will not affect educational loans in most jurisdictions unless the court specifically orders a discharge. Note, however, that a completed chapter 13 plan including the loan in the plan will discharge the loan.[18]

Fines levied by governmental units which are not in the nature of compensation for loss are also exempted from discharge.[19] Debts to colleges and universities other than educational loans or fines generally are dischargeable and therefore such debts will probably be voided by the general discharge.

The discharge injunction states that a discharge under the Bankruptcy Code operates as a bar against any act to collect, recover or offset the discharge debts against that debtor.[20] Refusal to permit students to order or gain access to official transcripts after discharge of all debts clearly violates the discharge injunction.[21] The argument that refusal to release transcripts is not an action, but a failure to act has been rejected.[22] Congress intended this

11. §1301(c) and (d). *See* In re Brown, 12 B.R. 885 (Bkrtcy N.D. Ga. 1981) (codebtor stay does not prevent withholding transcript of student whose parents had filed a chapter 13 bankruptcy because the daughter received the benefit of the education).

12. §362 (c). The codebtor stay lasts until the case is closed, dismissed, or converted to a chapter 7 case. §1301 (a)(2).

13. §1322 (c).

14. §524 (a)(2).

15. Whenever a debtor has received a discharge, an attorney should be consulted before withholding transcripts. It is impossible to adequately cover the complex issue of the dischargeability of student loans here. For further discussion, *see* Ayres and Sagner, *The Bankruptcy Reform Act and Student Loans: Unraveling New Knots*, 9 Journal of College and University Law 361, 367-388 (1982).

16. §523 (a)(8); *In re Wright*, 7 B.R. 197 (Bkrtcy N.D. Ala. 1980); *Massachusetts Higher Educ. Asst. Corp. v. Taylor*, 459 N.E.2d 807 (Mass. 1984); *but cf.* Ayres and Sagner, *The Bankruptcy Reform Act and Student Loans: Unraveling New Knots*, *supra*, at 384-388, where the authors note that some courts require that the issue be raised by the debtor or the university during the action, or that the university petition for relief from the discharge injunction before continuing collection activities after discharge. While the action is pending either the debtor or the institution may petition for a determination of the dischargeability of the loan to eliminate the uncertainty.

17. §1328 (b).

18. §523 (a); §1328 (a); *In re Lambert*, 10 B.R. 223 (Bkrtcy E.D. N.Y. 1981).

19. §523 (a)(7).

20. §524 (a)(2).

21. *Parraway v. Andrews University*, 50 B.R. 316 (W.D. Mich. 1984).

22. *Lanford v. Macalester College*, 10 B.R. 132 (Bkrtcy D. Minn. 1981).

section to ensure that the debtor "will not be pressured in any way" to repay discharged debts.[23]

Creditors who engage in efforts to collect on discharged debts subject themselves to possible fines and findings of contempt of court.[24]

It should be no surprise that the Bankruptcy Code prohibits withholding of transcripts after entry of a discharge. The purpose of a discharge is to grant a fresh start to the debtor free of the burdens of the discharged debts. Since withholding transcripts affects the ability to gain further education and employment, courts will take a dim view of such a tactic.

The Anti-Discrimination Provisions of the Bankruptcy Code

Section 525 (a) of the Bankruptcy Code provides that *governmental units* may not "deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, or similar grant to . . . or discriminate with respect to employment against" someone solely because he or she has filed for bankruptcy or received bankruptcy relief. Section 525 (b), added in 1984, provides that *private entities* may not discriminate against bankruptcy debtors with respect to employment. These provisions apply any time after the filing of a bankruptcy action and even after discharge. There are cases holding that the anti-discrimination clauses prevent withholding of transcripts by public institutions during the pendency of a case.[25] There are also cases under prior law which held that public colleges and universities could not discriminate against students whose debts were discharged by withholding their transcripts.[26] Whether private institutions are prevented from withholding transcripts by section 525 (b) remains unresolved. However, these issues are unimportant as far as withholding transcripts is concerned. The anti-discrimination provisions duplicate the stay provisions and the discharge injunction. The stay provisions prevent withholding during the pendency of a bankruptcy action. The discharge injunction prevents withholding after discharge of all debts. Thus, the only real question is whether the anti-discrimination provisions affect withholding of transcripts when the case is no longer pending and where there has not been a discharge of all debts. The answer is that they do not.

A federal appeals court has ruled that withholding a transcript did not violate section 525 (a) where the student had received a general discharge, but one which did not affect student loan obligations.[27] The court noted that Congress had exempted student loans from discharge in certain cases to prevent bankruptcy law from damaging the integrity of student loan programs. The court concluded that section 525 did not prevent withholding transcripts as a means of *undischarged* student loans.

Although there are especially strong reasons for permitting actions to collect educational loans when they have not been discharged, any non-discharged debt should be enforceable and therefore collectible by the creditor. Thus, it is generally permissible to

23. House Report No. 95-595 to accompany H.R. 8200, 95th Cong. 1st Sess. (1977), p. 366.

24. *In re Myers*, 18 B.R. 362 (Bkrtcy E.D. Va. 1982).

25. *E.g., In re Reese*, 38 B.R. 681, 683 (Bkrtcy N.D. Ga. 1984).

26. *Handsome v. Rutgers University*, 445 F.Supp. 1362 (D. N.J. 1978); *Lee v. Bd. of Higher Ed.*, 1 B.R. 781 (S.D. N.Y. 1979). These cases are probably still valid. Section 525 was originally enacted in 1978 to codify the holding in *Perez v. Campbell*, 402 U.S. 637, 91, S.Ct. 1704, 29 L.Ed.2d 233 (1971). House Report No. 95-595 to accompany H.R. 8200, 95th Cong. 1st Sess. (1977), p. 366. *Perez* held that a state could not refuse to reinstate the license of a driver solely because the driver had not paid a discharged judgment arising out of an automobile accident. Before section 525 became effective, *Handsome* and *Lee* relied on *Perez* in holding that withholding of transcripts was impermissible.

27. *Johnson v. Edinboro State College*, 728 F.2d 163 (3rd Cir. 1984).

withhold transcripts whether or not the surviving debt is an educational loan.

Summary

There are three rules to follow when dealing with the question whether to withhold transcripts of a bankruptcy debtor. The first is that a transcript should not be withheld during the pendency of a bankruptcy action without acquiring relief from the stay. The second is that if a discharge of all debts has been granted to the debtor, schools should not deny access to or orders of transcripts. The third is that it is permissible to deny transcripts where the case is no longer pending before the court and educational debts were not discharged, especially if the underlying obligation is a student loan.

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This is the first in a series of publications from NACUA, an organization of colleges and universities joined together for mutual assistance in identifying and resolving legal problems.

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July 1986

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